## How will new public shareholding norms impact mkts?

In its recent move, the government raised the threshold for public shareholding in listed companies to 25%. With this, companies where the public holding is less than 25%, will have to reach the minimum level by an annual addition of not less than 5%. If they fail to do that, they will have to restore the 25% public holding in one year.

These shareholding norms, S Ramesh, COO, Kotak Investment Banking, says will lead to deeper and liquid markets. “We will see heightened capital market activity. Also higher retail portion may lead to some instability.”

However, for Siddharth Shah of Nishith Desai and Associates the government’s move is not a surprise. “This may lead to a lot more pre-initial public offer (IPO) deals,” he says.

***Below is a verbatim transcript of the interview. Also watch the accompanying video.***

**Q: Is the market ready to absorb that kind of paper which might come in given the amount that the public sector companies may have to dilute their promoter holding by?**

**Ramesh:** At a strategic intent level, this is a positive measure for the Indian capital markets because as you recognize this is paving the foundation for a deeper more liquid markets.
In the past we all know there has been feedback from investors about high impact cost. There have been a number of stocks where liquidity has been a concern. So first at a strategic intent level let's start from there.

The second impact that I see quickly its going to heighten capital market activity be it FPO's, IPO's maybe QIP's, block trade, etc. but the other side, the flip side of this is a little bit of stock over hang. So we will have to sort of digest that.

Coming to you question on new paper, for the IPO markets there is going to be a more supply of paper. In the short to medium term given the sentiments of the retail investors have not been very strong in the recent past, this means there is going to be a bigger tranche for retail investors. So that's going to be a concern. Again on the positive side it's going to put owners on the capital market players and the insurance for more reasonable pricing because they have to clear a larger tray. So that's the positive side that I see of this regulation.

_PAGEBREAK_

**Q: The big question remains ability to absorb. Preliminary reports on this subject indicate that we go from what we have right now which is about 2% of outstanding market cap to over 5% in the medium term. Does the market have the capacity to absorb that kind of paper in terms of equity issuances?**

**Ramesh:** In the short to medium term supply of paper is going to be more. I just want to go back from our memories from 2004 and in the last five years, I think the market has steadily kept increasing. So while we see those occasional blurbs driven more by global liquidity and events my sense is that things will fall into place if we take a medium term perspective. Hence, I mentioned about more reasonable pricing which will be the paving or the corner stone for the paper to get absorbed.

**Q: A lot of the talk till now has been focused about the PSU companies and how they may choose to get this norm into place. For the private sector companies, do you think the more elegant way to do it just might be to do a QIP which does not help anyone and in particularly not liquidity in the primary market?**

**Shah:** The move here by the government actually is not truly a surprise because this has been on the cards for many years and it almost came to being enforced in 2008 just before the markets tang. So in one sense the markets have always expected this. To a great extent in the long run this is likely to create a deeper capital market as Ramesh pointed out and possibly a much better price discovery which is what the regulators are really looking at.

For private sector, this might create a bit of an overhang in terms of forced dilution by promoters which again maybe an issue. So many of them may actually, you may see a lot more or pre-IPO deals or post QIP offering or follow on offerings. So it is going to create a bit of an overhang in my view in the short run, but in the long run it should achieve the objective of creating much more efficient and deeper capital markets.

**Q: What about the multi national companies because they typically have global norms governing how much they would want to dilute in any particular geography? Do you think they will also dilute their parent company holding or many of them might chose to just delist the companies out of India?**

**Shah:** We might see some of these companies especially the MNC’s who may actually opt for delisting rather than really increasing the public float. So in that sense there maybe a situation where the retail investors may actually get an exit from some of the better performing MNCs. That is the trend which I foresee some of them would adopt as against the dilution. As you rightly pointed out some of them are governed by their own charters in terms of how much of dilution they would be comfortable with.

In the long run I would still think companies who are looking at the Indian markets from a longer term perspective and the fact that they are playing in the Indian markets would need to comply with these requirements as many other markets also imposed similar minimum public float requirement.

_PAGEBREAK_

**Q: Are you clear that ruling which has come over the weekend means that all public sector listed entities would have to comply with this, as in the large listed public sector entities or even some of the public sector banks where the government holding might be more than 75%?**

**Shah:** The policy has very clearly removed any distinction between PSU and private sector. To that extent they have created a level playing field. Unless there is any rethink on that front with looking at the market conditions and situations this point the policy seems to apply equally across the PSU and private sector.

**Q: On MNCs, do you think that might be the more likely outcome or delisting rather than an upping in terms of public shareholding?**

**Ramesh:** I would actually say that it would be not a 50-50 but a mixed bag. There are foreign companies who would look at Indian capital markets from a valuation arbitrage because their subsidiaries are getting well valued. Secondly, as their India plans set to go up I think some of them will understand that it is inevitable that they will have to go higher than their norms that they are comfortable with. From that perspective, you will have a basket of companies which will probably delist but there will be another basket of companies which will deepen the liquidity of their stock.

**Q: We were speaking to a banker the other day who pointed out that there has been a lull lately in the kind of offerings they have been hitting the market. What are you hearing basically in terms of sentiment appetite or even leaning towards these issues? Did we see the big first blush at the start of 2010, is that waning now?**

**Shah:** Yes. We have definitely experienced some amount of slow down in the capital market activity. The performances of some of the recent IPOs support that sentiment as well. To that extent this move moving from the government at this time might create a bit of an equity overhang in the short run which clearly would mean that retail participation again is a big concern. So people may opt for more QIPs which may actually disserve the purpose of creating because there may be from a liquidity perspective may not necessarily create the desired level of liquidity as with the public offerings but we do see a little waning of sentiment in terms of IPOs.

**Q: Specially on the public sector front, do you see the government now privatizing its calendar for the next 12 months giving priority to some of the existing listed companies like NTPC, NMDC, Power Grid, those kind of names to do and do 5% FPOs and raise money or do you think it will also want to do the large IPOs like Coal India which seem to be because if you put altogether you are talking about USD 15-17 billion of government float?**

**Ramesh:** It is clear that the numbers show that it is a challenging number. Many of these PSU companies are large monopoly players, great fundamentals. At one end, the fundamentals are likely to attract investors. The second point that I want to say is the smaller universe of PSU companies where the float has already gone up quite a bit. For example if you saw REC the float is gone up through the last new issue and the disinvestment that was done.

They will have to go back to the drawing board. There are issues like Coal India they are already announced. Some kind of privatizing of the calendar will happen. I believe they will do well and we should wait to see how they come up with. I do not think that by itself a very